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No. 99-1792

Supreme Court, U.S.
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In the
SUPREME COURT OF THE UNITED STATES
October Term, 2000

DIRECTOR OF REVENUE OF MISSOURI,
Petitioner,

v.

CoBANK, ACB, as Successor to the
National Bank for Cooperatives,
Respondent.

On Writ of Certiorari
to the Supreme Court of Missouri

# BRIEF FOR THE PETITIONER

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## QUESTION PRESENTED

May states tax the income of the National Bank of Cooperatives, a congressionally designated federal instrumentality, pursuant to 12 U.S.C. § 2134?

## PARTIES TO THE PROCEEDING

All of the parties to this proceeding are listed in the caption.



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# BRIEF FOR THE PETITIONER

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## OPINIONS BELOW

The opinion of the Supreme Court of Missouri (Petition Appendix (P.A.) A-1-A-4), entered on January 25, 2000, is reported at 10 S.W.3d 142. The opinion covers two appeals, one by three "production credit associations" (PCAs), and one by a "bank for cooperatives" (BFC), CoBank. The decision of Missouri's Administrative Hearing Commission (AHC) is not reported; it is printed at P.A. A-5-A-16.

## JURISDICTION

The Supreme Court of Missouri entered its judgment on January 25, 2000. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257.

## CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

1. U.S. Const. art. VI., cl. 2:

> This constitution, and the laws of the United States which shall be made in pursuance thereof, and all treaties made or which shall be made under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the constitution or laws of any state to the contrary notwithstanding.

12 U.S.C. § 2134 (1988):

> Each bank for cooperatives and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such bank shall be exempt, both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any State, territorial, or local taxing authority, except that interest on such obligations shall be subject to Federal income taxation in the hands of the holder.



Mo. Rev. Stat. § 143.071 (1994):

> 1. For all tax years beginning before September 1, 1993, a tax is hereby imposed upon the Missouri taxable income of corporations in an amount equal to five percent of Missouri taxable income.
>
> 2. For all tax years beginning on or after September 1, 1993, a tax is hereby imposed upon the Missouri taxable income of corporations in an amount equal to six and one-fourth percent of Missouri taxable income.

Mo. Rev. Stat. § 143.441 (1994) (in pertinent part):

> 1. The term "corporation" means every corporation, association, joint stock company and joint stock association organized, authorized or existing under the laws of this state and includes:
>
> (1) Every corporation, association, joint stock company, and joint stock association organized, authorized, or existing under the laws of this state, and every corporation, association, joint stock company, and joint stock association, licensed to do business in this state, or doing business in this state, and not organized, authorized, or existing under the laws of this state, or by any receiver in charge of the property of any such corporation, association, joint stock company or joint stock association;
>
> . . . .

2. The tax on corporations provided in subsection 1 of section 143.431 and section 143.071 shall not apply to:

. . .

(5) Any other corporation that is exempt from Missouri income taxation under the laws of Missouri or the laws of the United States.

## STATEMENT OF THE CASE

This case addresses state taxation of Banks for Cooperatives – entities established by federal charter that make loans to agricultural cooperatives. *See* H.R. Rep. No. 425, 99th Cong., 1st Sess. 5 (1985), *reprinted in* 1985 U.S.C.C.A.N. 2587, 2591. Like Production Credit Associations and other similar entities, they are part of the Farm Credit System, the establishment of which began with the creation of Federal Land Banks in 1916. The Federal Farm Loan Act, Pub. L. No. 64-158, § 4, 39 Stat. 360, 362 (1916). The System is regulated by the Farm Credit Administration, an independent regulatory agency of the United States government. H.R. Rep. No. 425 at 5, 1985 U.S.C.C.A.N. at 2592.

From the beginning, Congress comprehensively specified the tax treatment of each type of Farm Credit System institution. Congress began by giving the original Federal Land Banks a broad exemption from taxation. That exemption applied to the banks themselves, to their assets, and to their income. Pub. L. No. 64-158, § 26, 39 Stat. at 380. As to real property taxes, however, Congress clearly distinguished the Land Banks from federal agencies generally: federal agency lands were not taxed; Land Bank-owned land was. *Id.*

Over the years, as the Farm Credit System grew in size



and scope, Congress continued the practice of specifying tax treatment. For example, when Congress created the Federal Intermediate Credit Banks in 1923, it gave them the same broad statutory tax exemption possessed by Land Banks since 1916. The Federal Farm Loan Act, Pub. L. No. 67-503, § 210, 42 Stat. 1454, 1459 (1923). When Congress streamlined the system in 1987 by merging the Land Banks and the Intermediate Credit Banks, it made only slight changes to 1916 wording. *See* 12 U.S.C. § 2023.

Banks for Cooperatives (BFCs) were authorized by the Farm Credit Act of 1933, Pub. L. No. 73-98, § 40, 48 Stat. 257, 264 (1933). BFCs make loans to agricultural, aquatic, and rural utility cooperatives and provide financial services to cooperatives engaged in international trade. H.R. Rep. No. 425 at 5, 1985 U.S.C.C.A.N. at 2592. When they were first created, the BFCs were capitalized and owned entirely by the federal government. Over the years, however, borrowers achieved what Congress had intended (S. Rep. No. 124, 73rd Cong., 1st Sess. 2 (1933)): the government's stock was retired, and ownership was vested entirely in private hands. "All government and seed money advanced was paid back to the United States Treasury as of 1968." H.R. Rep. No. 425 at 5, 1985 U.S.C.C.A.N. at 2591.[1]

When it created BFCs, Congress maintained its practice of specifying the scope of the BFCs' tax immunity. But the tax

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[1]BFCs initially were capitalized by the United States out of the revolving fund from which the Federal Farm Board previously made loans to cooperatives under the Agricultural Marketing Act of 1929. Under the provisions of the Farm Credit Act of 1955, the government capital in the BFCs has been systematically retired by the creation of permanent capital provided by users of the BFCs. The first of the BFCs to retire all of its government capital did so in 1965 and the last in 1968. H.R. Rep. No. 593, 92nd Cong., 1st Sess. 9 (1971), *reprinted in* 1971 U.S.C.C.A.N. 2091, 2099.

exemption that Congress specified for BFCs differed from that granted to the Land Banks and the Intermediate Credit Banks. The exemption began with the declaration – still in the law today – that "Banks for Cooperatives . . . and their obligations [are] instrumentalities of the United States." Pub. L. No. 73-98, § 63, 48 Stat. at 267. What followed in that same sentence was a specific exemption for the financial instruments of the BFCs: "and as such, any and all notes, debentures, bonds, and other such obligations issued by [BFCs] shall be exempt both as to principal and interest from all taxation . . . imposed by the United States or by any State, Territorial, or local taxing authority." *Id.* Congress then gave BFCs another broader but temporary exemption: "[BFCs], their property, their franchises, capital, reserves, surplus, and other funds, and their income, shall be exempt from all taxation now or hereafter imposed by the United States or by any State, Territorial, or local taxing authority."[2] *Id.* The provision concluded with what we would now call a "sunset" clause: the broad exemption for any BFC expired once the government was no longer a stockholder in that BFC. *Id.* Thus the government temporarily lent its credit and resources to make each BFC viable, and made states and local governments share the burden by precluding them from imposing taxes on that BFC, other than property taxes, for as long as BFC stock was owned by the federal government.

Congress substantially rewrote the Farm Credit System statutes in the Farm Credit Act of 1971, but left unchanged the differing tax exemptions granted to the various system institutions. *See* Pub. L. No. 92-181, §§ 1.21, 2.8, 2.17, 3.13, 85 Stat. 583, 590, 597, 602, 608-09 (1971). Under the 1971 Act

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[2]Notably, even that broad exemption contained an exception for property taxes: "except that any real property and any tangible personal property . . . shall be subject to Federal, State, Territorial, and local taxation to the same extent as other similar property is taxed." *Id.*



there was still a possibility that the broad, contingent tax exemption might be invoked by a BFC: the 1971 Act provided that the revolving fund established in the Agricultural Marketing Act, as amended, Pub. L. No. 87-494, 76 Stat. 109, would be preserved and made available for the temporary investment in stock of BFCs by the Governor of the Farm Credit Administration. Farm Credit Act of 1971, Pub. L. No. 92-181, §§ 4.0 (a), 4.1 (b), 85 Stat. 583, 609-10 (1971); H.R. Rep. No. 593 at 23-24, 1971 U.S.C.C.A.N. at 2113-14.

Just as the savings and loan crisis prompted reform of the federal deposit insurance program, a crisis in American agriculture persuaded Congress to restructure the Farm Credit System in 1985. *See generally Colorado Springs PCA v. Farm Credit Admin.*, 967 F.2d 648, 650-52 (D.C. Cir. 1992). The restructuring was designed to accomplish the following:

I. Give the Farm Credit System broader authority to use its own resources to shore up weak system units.

II. Reshape the Farm Credit Administration, an independent federal agency, to make it a stronger, arm's-length regulator of the System.

III. Provide new protection for system borrowers.

IV. Provide that if the Farm Credit Administration certifies that the System needs financial aid and has made the maximum practicable effort to deal with financial stress, the Secretary of the Treasury would have discretionary

> power to backstop the System's finances by purchasing obligations of a System unit called the Farm Credit System Capital Corporation.

H.R. Rep. No. 425 at 1, 1985 U.S.C.C.A.N. at 2587-88.

That restructuring eliminated the position of "Governor" of the Farm Credit Administration. *Id.* at 28-29, 1985 U.S.C.C.A.N. at 2615. And it eliminated the power of the Farm Credit Administration to make investments in stock of BFCs out of the revolving fund. *Compare* Pub. L. No. 92-181, § 5.18(10), 85 Stat. at 622 (1971) *with* Farm Credit Amendments Act of 1985, Pub. L. No. 99-205, § 5.17(8), 99 Stat. 1678, 1692 (1985). This change was designed to eliminate the Farm Credit Administration's involvement in the management activities of the System institutions in order to make it a stronger, arm's-length regulator of the system. *See* H.R. Rep. No. 425 at 23-24, 1985 U.S.C.C.A.N. at 2609-10.

Because the title "Governor" and a reference to the Governor holding stock appeared in the last sentence of the BFC tax exemption statute (the "sunset" clause), the restructuring required revision of that law.[3] Within a section of the 1985 Amendments titled "Technical and Conforming Amendments," the statute struck references to "Governor" in

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[3]In early versions of the bill, the Farm Credit Administration still had the power to make investments in the stock of BFCs. And instead of striking the last two sentences of § 3.13, only the word "Governor" was stricken from the last sentence or sunset clause. Thus, when the bill retained the possibility for the Farm Credit Administration to own stock in BFCs, the exemption and sunset clause remained in the bill. *See* H.R. 3792, 99th Cong., 1st Sess. §§ 5.12(7)(a)(8), 205(e)(10) (November 20, 1985); S. 1884, 99th Cong., 1st Sess. §§ 106(c)(1), 110(8), 131 Cong. Rec. S16698-01 (December 3, 1985).



twenty-seven sections of the law and references to the Governor holding stock in twenty-three sections of the law. Pub. L. No. 99-205, § 205, 99 Stat. at 1703-1707 (1985).[4] The stricken last two sentences of § 3.13 contained the broad exemption from taxes followed by the sunset clause:

> Such banks, their property, their franchises, capital, reserves, surplus, and other funds, and their income shall be exempt from all taxation now or hereafter imposed by the United States or by any State, territorial, or local taxing authority; except that interest on the obligations of such banks shall be subject only to Federal income taxation in the hands of the holder thereof pursuant to the Public Debt Act of 1941 (31 U.S.C. 742(a)) and except that any real and tangible personal property of such banks shall be subject to Federal, State, territorial, and local taxation to the same extent as similar property is taxed. The exemption provided in the preceding sentence shall apply only for any year or part thereof in which stock in the bank for cooperatives is held by the Governor of the Farm Credit Administration.

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[4]Included among these revisions with regard to BFCs are: striking out "except for stock held by the Governor" in § 3.3(e); striking out a sentence referring to nonvoting stock held by the Governor in § 3.5; striking out subsection (a) of § 3.11 dealing with the application of savings "at the end of each fiscal year when said bank shall have stock outstanding held by the Governor"; striking out the precursor in § 3.11 (b) of "Whenever at the end of any fiscal year a bank for cooperatives shall have no outstanding capital stock held by the Governor"; striking out the references in § 3.12 to "any stock held by the Governor of the Farm Credit Administration at par" and "stock held by the Governor of the Farm Credit Administration"; and, finally, "striking out the last two sentences of section 3.13." Pub. L. No. 99-205, § 2.05, 99 Stat. at 1705.

Pub. L. No. 92-181, § 3.12, 85 Stat. at 609 (1971).

What remained, with minor subsequent changes, was the tax exemption for BFCs codified at 12 U.S.C. § 2134. Congress, having deleted the broad exemption in the original statute for which no BFC remained eligible, preserved the tax-exempt status only of investment vehicles issued by BFCs:

> Each bank for cooperatives and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such associations shall be exempt, both as to principal and interest, from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any State, territorial, or local taxing authority, except that interest on such obligations shall be subject to Federal income taxation in the hands of the holder.

12 U.S.C. § 2134 (1988).

The legislative history of the Farm Credit Amendments Act of 1985 never suggests a change in tax immunity in its forty-nine page report. The House Agricultural Committee makes no mention of the taxable status of BFCs, let alone an expansion of the scope of tax exemptions for BFCs. H.R. Rep. No. 425 at 1-49, 1985 U.S.C.C.A.N. at 2587-2636.[5] No Senate

[5]The congressional committee described the purpose of the "technical and conforming" amendments, which included striking the last two sentences of § 3.13, as follows:

> Section 205 contains numerous technical and conforming amendments to the provisions of the Farm Credit Act of 1971 affected by changes in the basic powers, duties and authorities of the Farm Credit Administration. This section would amend the appropriate provisions of the Act to delete the requirement for specific approval by the Farm Credit Administration of certain activities of the banks and associations and by deleting the general authority of the Farm Credit Administration to supervise system institutions. These changes are consistent with one of the major purposes of the legislation which is to establish the Farm Credit Administration as an arms length regulator of the system institutions and to take it out of certain activities of the system which would involve it in management discretion of such institutions.
>
> This section also contains amendments which conform specific sections of the Act to the change made by the merger of the revolving funds and the elimination of the authority to make separate investments in individual institutions. As amended by the Act, the Farm Credit Administration may only make investments from the section 4.0 revolving fund in the Farm Credit System Capital Corporation. This section also contains conforming amendments to other sections of the Act which delete the individual authorities of the system institutions to exercise authorities delegated to them by the Farm Credit Administration.
>
> Finally, this section deletes references to the Governor of the Farm Credit Administration and the Federal Farm Credit Board, since such office and board will no longer exist, and substitutes for such provisions, a reference to the "Farm Credit Administration."

H.R. Rep. No. 425 at 28-29, 1985 U.S.C.C.A.N. at 2615.



report was submitted with the legislation. No one made mention of the tax status of BFCs or an expansion of the scope of tax exemptions for BFCs in either the House or Senate proceedings and debates on the Act. *See* 131 Cong. Rec. S16698-01 (December 3, 1985), 131 Cong. Rec. H11506-03 (December 10, 1985), 131 Cong. Rec. H11546-02 (December 10, 1985), 131 Cong. Rec. S17748-02 (December 17, 1985),

131 Cong. Rec. H12529-01 (December 18, 1985).

Following the 1985 Amendments, the National Bank for Cooperatives (NBC) filed Missouri corporate income tax returns and paid income tax for tax years through 1994. Joint Appendix (J.A.) A-13-A-15, A-29.

In 1995, CoBank, as successor to NBC,[6] filed amended returns on behalf of NBC, seeking refunds of income tax paid for 1991 through 1994. J.A. A-8, A-25. CoBank did not argue that it was excluded from taxation by Missouri law. It relied, instead, on federal immunity. The Missouri Director of Revenue denied those claims in pertinent part, imposing Missouri's corporate income tax on CoBank pursuant to Mo. Rev. Stat. § 143.071 (1994). J.A. A-16-A-22, A-31-A-37.

CoBank filed a complaint in Missouri's Administrative Hearing Commission (AHC), challenging that decision. J.A. A-6-A-37. The AHC upheld the Director's denial. P.A. A-16. For jurisdictional reasons, it did not reach CoBank's immunity claim. *Id.*

CoBank then appealed to the Missouri Supreme Court, which decided CoBank's immunity claim. It held that BFCs are federal instrumentalities, that federal instrumentalities cannot be taxed absent a clear and express statutory waiver of immunity, that the language 12 U.S.C. § 2134 does not contain express consent to state taxation, and thus that the State of Missouri could not impose state income taxes on BFCs. P.A. A-2-A-3.

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[6] The National Bank for Cooperatives, which operated in Missouri, was formed by the mergers of many of the existing BFCs in 1989. CoBank was formed in 1995 from a consolidation of NBC with two other entities. In 1999, the sole remaining independent BFC also merged into CoBank.



Petitioner filed a Petition for Writ of Certiorari in this Court seeking to correct the decision of the Missouri Supreme Court. On June 26, 2000, this Court granted the petition. J.A. A-59.

## SUMMARY OF ARGUMENT

The Missouri Supreme Court's decision was based on the doctrine of implied immunity from state taxation for federal instrumentalities. In its first century, that doctrine was applied broadly, and the Missouri Supreme Court's demand for an express waiver of immunity would have made sense. But in its second century, the application of implied tax immunity has been significantly circumscribed. Today, only those entities that are so closely associated with the government that the two are indistinguishable can claim implied immunity from all state taxes.

Of course, Congress may also provide that other federal instrumentalities it authorizes or creates shall be immune from some or all state or local taxes. But for those entities, the immunity is defined by statute, not by reference to implied immunity.

Although BFCs are, by express congressional designation, "federal instrumentalities," this label does not establish a congressional intent to entitle them to the complete freedom from state taxation the Government itself enjoys, particularly where that label is applied in the context of a far narrower grant of immunity. BFCs are easily distinguishable from the Government itself, and they do not qualify for implied, absolute tax immunity merely because they have explicitly been given certain specified rights and privileges as "federal instrumentalities." The Missouri Supreme Court thus erred by insisting on an express congressional waiver of immunity, and

by belittling the significance of Congress's limited grant of immunity.

BFCs must look to Congress and statutes for immunity from state taxation. But the grant of tax immunity to BFCs is limited to immunity from the taxation of BFCs' notes, debentures, and other obligations. Thus Missouri can impose income and other taxes unless and until Congress adds them to the list of proscriptions.

## ARGUMENT

### A. Congressionally-chartered entities designated as "federal instrumentalities" do not enjoy implied immunity from state taxes, unless they are so closely connected to the Government that the two cannot realistically be viewed as separate entities.

The doctrine of implied tax immunity that forms the foundation for the Missouri Supreme Court's decision originated in *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819). There, this Court ruled not only that the Second Bank of the United States – a federally chartered bank partially owned by the United States – was constitutionally established, but also that the Supremacy Clause prevented the states from attempting to tax it out of existence through the imposition of discriminatory taxes upon the Bank's notes and other instrumentalities: "[T]he states have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control, the operations of the constitutional laws enacted by congress to carry into execution the powers vested in the general government." *Id.* at 436.

In the first century after *M'Culloch*, the doctrine of implied intergovernmental tax immunity was rapidly expanded



to prohibit even those nondiscriminatory state taxes that only marginally and incidentally impacted federal activities, such as taxes on the income of federal employees, *Dobbins v. Commissioners of Erie County*, 41 U.S. (16 Pet.) 435 (1842), and on income generated by property leased from the federal government, *Gillespie v. Oklahoma*, 257 U.S. 501 (1922). Beginning in the 1930's, however, as the scope of federal governmental activities expanded, this Court progressively narrowed the scope of this implied immunity, allowing, for instance, state taxation of income received from services provided to the federal government, *James v. Dravo Contracting Co.*, 302 U.S. 134 (1937), and of the income of federal employees, *Graves v. New York ex rel. O'Keefe*, 306 U.S. 466 (1939). *See Jefferson County, Alabama v. Acker*, 527 U.S. 423, 436-37 (1999) ("Until 1938, the intergovernmental tax immunity doctrine was expansively applied . . . . Since *Graves*, we have reaffirmed 'a narrow approach to governmental tax immunity . . . .'") (quoting *United States v. New Mexico*, 455 U.S. 720, 735 (1982)).

This narrowing trend culminated in *United States v. New Mexico*, 455 U.S. 720 (1982) (*New Mexico*), in which this Court comprehensively reexamined the constitutional bases and proper scope of the implied intergovernmental tax immunity doctrine. Recognizing the "confusing nature of [its] precedents" and the inconsistent results that the implied immunity doctrine had produced, this Court unanimously announced a return to the "underlying constitutional principle," *i.e.*, that "a State may not, consistent with the Supremacy Clause, lay a tax 'directly upon the United States.'" *Id.* at 733 (quoting *Mayo v. United States*, 319 U.S. 441, 447 (1943)). Although the Court noted that *M'Culloch* "could, and perhaps should" be read to prohibit only taxes discriminating against the federal government or its instrumentalities, the Court reaffirmed that the implied immunity doctrine that had arisen in

*M'Culloch's* wake reflected "a deep instinct" that the federal system also required some form of absolute governmental tax immunity, even from non-discriminatory taxes. 455 U.S. at 733-34. Under the modern federal structure, however, this immunity doctrine has taken on "essentially symbolic importance," such that its scope is sharply limited. *Id.* at 735.

After *New Mexico*, any court considering whether a federal instrumentality can rely on implied intergovernmental tax immunity must first decide not just whether the entity in question is "an agency or instrumentality" of the Government, but whether it is "so closely connected to the Government that the two cannot realistically be viewed as separate entities, at least so far the activity being taxed is concerned." *Id.* at 735. "[T]o resist the State's taxing power, a private taxpayer must actually 'stand in the government's shoes.'" *Id.* at 736 (quoting *City of Detroit v. Murray Corp.*, 355 U.S. 489, 503 (1958) (opinion of Frankfurter, J.)). Thus, status as an agent of the government does not entitle a taxpayer to immunity; instead, the taxpayer must be "so intimately connected with the exercise of a power or the performance of duty by the government that [taxation] would be a direct interference with the functions of government itself." *Id.* at 455 U.S. 736. The only entities automatically entitled to immunity are those that are "virtually an arm of the Government," or have been "incorporated into the Government structure." *Id.* at 736-37.

This rule, narrowly circumscribing the intergovernmental tax immunity doctrine, vindicates the Supremacy Clause while recognizing the important countervailing interest in respecting state sovereignty. Because "the principal purpose of the immunity doctrine" is to "forestall[] clashing sovereignty," a rule limiting the implied immunity doctrine to cases where the states attempt to "lay[] demands directly on the Federal Government" is "a narrow



approach," which "accords with competing constitutional imperatives, by giving full range to each sovereign's taxing authority." *Id.* at 735-36. This narrow approach also has the benefit of placing the primary responsibility for determining which aspects of state taxation might burden federal operations where that responsibility belongs – on Congress:

> If the immunity of federal contractors is to be expanded beyond its narrow constitutional limits, it is Congress that must take responsibility for the decision . . . . And this allocation of responsibility is wholly appropriate, for the political process is uniquely adapted to accommodating the competing demands in this area. But absent congressional action, we have emphasized that the States' power to tax can be denied only under the clearest congressional mandate.

*Id.* at 737-38 (internal citations and quotation marks omitted).

The highly political nature of the process of accommodating the financial needs of competing sovereignties also requires that Congress, and not the executive or the judiciary, be the branch of the federal government primarily responsible for determining the bounds of intergovernmental tax immunity. *See id.* at 737 (condemning approach that allows "an immunity of constitutional stature" to be founded on the manner in which a "government functionary" draws up a particular contract); *Arizona Dept. of Revenue v. Blaze Constr. Co.*, 526 U.S. 32, 38 (1999) ("Whether to exempt [a federal contractor] from Arizona's transaction privilege tax is not our decision to make; that decision rests, instead with the State of Arizona and with Congress."). *M'Culloch* and *New Mexico*, combined, still permit Congress to determine the bounds of tax

immunity implicitly, *i.e.*, by giving an entity the attributes that permit it to partake of implied immunity under *New Mexico*. But this Court's recent decisions suggest that the judiciary should be reluctant to extend implicit immunity to non-governmental entities unless Congress has clearly endorsed that extension.

The fact that Congress has labeled an entity a "federal instrumentality" does not constitute such an endorsement – particularly where, as here, it is accompanied by a provision defining the instrumentality's tax immunity. Nor can the mere label, in terms of the *New Mexico* standard, conclusively establish that the labeled entity is such an integral part of the Government as to entitle it to the complete implied immunity from taxation that the Government itself enjoys. Thus in *Arkansas v. Farm Credit Servs.*, 520 U.S. 821 (1997) (*Farm Credit*), this Court rejected the idea that such a label vests an entity with the full range of governmental immunities.

Rather than converting an entity into an alter ego of the Federal Government, this Court held, use of the label "federal instrumentality" still left to Congress responsibility for defining an entity's ability to access government benefits and immunities: "An instrumentality of the United States can enjoy the benefits and immunities conferred by explicit statutes . . . without the further inference that the instrumentality has all of the rights and privileges of the National Government." *Id.* at 829.[7] As *Farm Credit* suggests, Congress may use the "federal

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[7]In that respect, the *Farm Credit* decision upholds the same important federalism principles that animated the narrow approach to intergovernmental tax immunity established in *New Mexico*:

> In our constitutional system, the power of the State to tax is a concurrent power. "That the power of taxation is one of vital importance; that it is retained by the States; that it is not abridged by the grant of a similar power to the government of the Union; that it is to be concurrently exercised by the two governments: are truths which have never been denied." *McCulloch v. Maryland*, 4 Wheat. 316, 425, 4 L.Ed. 579 (1819). The power to tax is basic to the power of the State to exist.

*Id.* at 826.



instrumentality" label to specify that an entity stands in the shoes of the Government for certain, explicitly defined purposes, without implying that such an entity becomes the Government for all purposes. Where the explicit statutory immunity accompanying the "federal instrumentality" label is a narrow one, Congressional endorsement of a sweeping implied immunity is plainly lacking, and the mere fact that Congress has used the words "federal instrumentality" does not, in and of itself, compel a different result.

Here, then, was the fundamental error committed by the Missouri Supreme Court: it ignored that teaching from *Farm Credit* and thus avoided having to decide whether Congress intended that BFCs should qualify for implied immunity under the *New Mexico* standard. For that court and for CoBank, that BFCs are congressionally-designated "federal instrumentalities" was enough to ensure them the benefits of implied immunity. Thus the Missouri Supreme Court held that the instrumentality designation implicitly creates the universal state tax immunity that the federal government itself enjoys, and then that any contrary implication may only be dispelled through clear and express language. P.A. A-2-A-3.

Contrary to this inflexible holding, this Court has never concluded that federal instrumentalities, whether labeled by Congress as such or not, should be deemed presumptively immune from state taxation on the strength of that

characterization alone. Rather, even when it has concluded that a particular entity is in fact a federal instrumentality, this Court has nevertheless undertaken to determine the federal purpose of the instrumentality, and has emphasized that the courts must look to how Congress defined the authority and character of the instrumentality to determine the scope of the instrumentality's immunity: "What governmental instrumental-ities will be held free from state taxation, though Congress has not expressly so provided, cannot be determined apart from the purpose and character of the legislation creating them." *Shaw v. Gibson-Zahniser Oil Co.*, 276 U.S. 575, 578 (1928). Thus, "[t]here are some instrumentalities which, though Congress may protect them from state taxation, will nevertheless be subject to that taxation *unless* Congress speaks." *Id.* at 581 (emphasis added).

Because this Court has never adopted a rule requiring express waivers of tax immunity for all federal instrumentalities, it has never suggested what the Missouri Supreme Court held: that congressional silence regarding a state tax means that tax cannot be imposed. Rather, "[t]he silence of Congress as to the subjection of its instrumentalities, other than the United States, to local taxation or regulation is to be interpreted in the setting of the applicable legislation and the particular exaction." *Mayo v. United States*, 319 U.S. 441, 448 (1943). And consideration of the "setting of the applicable legislation and the particular exaction" requires inquiry into the same factors that guide the question of whether that instrumentality is inherently constitutionally exempt: "[W]hen exemption from state taxation is claimed on the ground that the federal government is burdened by the tax, and Congress has disclosed no intention with respect to the claimed immunity, it is in order to consider the nature and effect of the alleged burden, and if it appears that there is no ground for implying constitutional immunity, there is equally a want of any ground



for assuming any purpose on the part of Congress to create an immunity." *Graves v. New York ex rel. O'Keefe*, 306 U.S. 466, 480 (1939).

Under *New Mexico* and *Farm Credit*, then, BFCs partake of implied immunity only if they show that their functions are "so intimately connected with the exercise of a power or the performance of duty by the Government that taxation of it would be a direct interference with the functions of government itself." *New Mexico*, 455 U.S. at 736. As discussed in part B, *infra*, CoBank cannot make that showing. Thus CoBank must show that Congress granted BFCs immunity from state income taxes. As discussed in part C, *infra*, CoBank cannot make that showing either.

### B. Because BFCs are not so closely connected to the Government that they cannot realistically be viewed as separate from the government and thus qualify for implied immunity from state taxes, the full extent of their tax immunity is defined by statute.

Particularly with respect to the activity being taxed here – the generation of income from making loans in competition with commercial banks – BFCs such as the National Bank for Cooperatives and its successor, CoBank, are not functionally indistinguishable from the federal government. Rather, they are wholly owned and operated by private entities and, most importantly for purposes of an income tax, their income is produced for the benefit of their (private) shareholders, and not for the benefit of the government or the public.

BFCs are, in this respect, indistinguishable from the production credit associations (PCAs) whose tax immunity was at issue in *Farm Credit*. The interests of BFCs, like the interests of PCAs, "are not coterminous with those of the

Government any more than most commercial interests." *Farm Credit*, 520 U.S. at 831. BFCs, like PCAs, "more closely resemble . . . private entities" than the federal government and its agencies, exercising no regulatory authority "but rather serv[ing] specific commercial and economic purposes long associated with various corporations chartered by the United States." *Id.* at 830-31.

As this Court concluded as to PCAs in *Farm Credit*, the interests of BFCs are not sufficiently identical to those of the government that they "cannot realistically be viewed as separate entities." Thus BFCs cannot qualify for implied immunity under the *New Mexico* standard.

**C. Congress has not granted BFCs immunity from state taxes, except those imposed on the BFCs' notes, debentures, and other obligations.**

CoBank can only claim immunity from state taxation, then, to the extent that such immunity has been granted by Congress. The extent of the grant of immunity to BFCs is unambiguous, and has been since the BFCs were first authorized nearly 70 years ago.

The original statute gave BFCs immunity for their notes, debentures, and obligations, denied immunity from property tax, and granted immunity temporarily from other state and local taxes. *See* p. 6, *supra*. Since 1985, BFCs have had immunity only as to their notes, debentures, and obligations. *See* pp. 9-10, *supra*. The statutory language leaves no "well-grounded doubt" to be "resolved in favor of the exemption." *Austin v. Board of Aldermen*, 74 U.S. (7 Wall.) 694, 699 (1868).

Nor can doubt be found in the statute's history. As



noted above, before 1985 Congress comprehensively defined the scope of BFC immunity: BFCs were immune from all state and local taxes (except property taxes) while the government was a stockholder; and they lost all their immunity, except for taxes on "notes, debentures, and other obligations," when the government's stock was retired. The 1985 amendments eliminated the "sunset" clause, which no longer had any effect because the government's stock had been retired since 1968 and the Farm Credit Administration no longer possessed the power to invest in the stock of BFCs. In eliminating the clause on which the sun had set, Congress did not eliminate its authorization of the states' power to tax BFCs. Nor was it entirely silent, as the Missouri Supreme Court presumes. Congress spoke through a combination of words (only "notes, debentures, and other obligations" are tax-exempt) and action (repeal of the broader, contingent, pre-1985 exemption).

Congress also spoke through its placement of section 2134 and the 1985 changes in a broader statutory scheme. *See Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 809 (1989) (the words of a statute must also be read in their context and with a view toward their place in the overall statutory scheme); *Gustafson v. Alloyd Co., Inc.*, 513 U.S. 561, 569 (1995) (a court must interpret the statute "as a symmetrical and coherent regulatory scheme"); *FTC v. Mandel Brothers, Inc.*, 359 U.S. 385, 389 (1959) (court must "fit, if possible, all parts into an harmonious whole."). Since 1916, Congress has comprehensively specified the tax treatment of each type of Farm Credit System institution. When Congress wished to grant an institution an unconditional exemption from all state and local taxes, except property taxes, it simply said so. *See* Pub. L. No. 64-158, § 26, 39 Stat. 360, 380 (1916) (Federal Land Banks), Pub. L. No. 67-503, § 210, 42 Stat. 1454, 1459 (1923) (Federal Intermediate Credit Banks), Pub. L. No. 92-181, § 1.21, 85 Stat. 583, 590 (1971) (Federal Land Bank

Associations). And since the 1985 Act, Congress has managed to say so again and again as it granted such exemptions to new entities. *See* 12 U.S.C. § 2023 (Farm Credit Banks), 12 U.S.C. § 2277a-12 (Farm Credit System Insurance Corporation), 12 U.S.C. § 2278a-11 (Assistance Board), 12 U.S.C. § 2278b-10 (Financial Assistance Corporation). If Congress had wished to grant BFCs an unconditional exemption in 1985, it undoubtedly knew how to do it. *See Brown v. Gardner*, 513 U.S. 115, 120 (1994) ("[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposefully in the disparate inclusion or exclusion." (internal citation omitted)). Indeed, in order to accomplish that result, Congress need only have deleted the sunset clause and left the broad exemption in the statute. Instead it struck both.

Congress did not speak to the contrary anywhere in the history of the 1985 Act. Rather than suggest that Congress intended to grant BFCs unique tax immunity, that record is completely silent on any change in the tax treatment of BFCs. The committee report and debates never mention the taxable status of BFCs, let alone an expansion of the scope of tax exemptions. The change to § 2134 is instead merely labeled a "technical and conforming" amendment. This characterization only makes sense if Congress merely intended to delete an exemption for which BFCs were no longer eligible. "Technical and conforming" could not describe an intent to radically change the tax status of BFCs and give them an unconditional exemption in lieu of a moribund exemption tied to government ownership of their stock. The "silence" thus speaks volumes – in opposition to CoBank's claim of a dramatic change.

The history of the Farm Credit Amendments further reveals an intent to render BFCs independent, private entities – the kind that obviously could not meet the *New Mexico*



standard. The purpose of the restructuring of the Farm Credit System in 1985 was to cut the ties between the Farm Credit Administration and the system banks and associations in order to make the Farm Credit Administration an arms-length regulator of the system. One such tie was the power of the Farm Credit Administration to invest in the stock of BFCs, a power eliminated in the 1985 Act. Thus, the history and purpose of the 1985 Act do not support a result in which BFCs are treated for tax purposes as if they stood in the shoes of the federal government. To the contrary, they support a conclusion that even if the BFCs qualified under the *New Mexico* standard before 1985 (which they did not), their government affiliation has since been significantly loosened.

There is nothing in the language of the current statute, in its evolution in the legislative history of the 1985 Act, nor even in logic to support the proposition that Congress returned to BFCs in 1985 the tax-exempt status they had enjoyed while owned in part by the United States. To the contrary, the extension of this position shows the perverted logic of the rule: it would give BFCs not just the tax benefits lost by BFCs many years ago, but benefits they had never enjoyed.

In that respect, the dramatic effect of the Missouri Supreme Court's ruling is best illustrated in the context of property taxes. Because Congress did not mention property taxes in its 1985 version of § 2134, the Missouri court's holding necessarily contemplates that property taxes would be among the taxes the BFCs need not pay. But Congress has clearly and consistently required federal instrumentalities in the Farm Credit System to pay property taxes – thus preserving an important source of revenue for rural governments and schools. *See* 12 U.S.C. § 2278a-11 (the Assistance Board must pay "taxes on real estate held by the Assistance Board to the same extent, according to its value, as other similar property held by

other persons is taxed"); 12 U.S.C. § 2278b-10 (same language for the Financial Assistance Corporation); 12 U.S.C. § 2023 (same language for the Farm Credit Banks); 12 U.S.C. § 2098 (same language for Federal Land Bank Associations).[8] BFCs were similarly required to pay property taxes before 1985 – even while wholly or partially owned by the United States, pursuant to language parallel to that applied to other Farm Credit System entities and later by virtue of having lost the protection of the broad tax exemption.

Now, as a result of the Missouri Supreme Court's ruling, BFCs (and PCAs, which have a parallel waiver statute) have become unique among federally-chartered, privately-owned financial institutions – the sole institutions not subject

[8] Congress has used similar language in defining the scope of immunity retained by federally-chartered financial institutions outside the Farm Credit System. *E.g.*, 12 U.S.C. § 531 (federal reserve banks); 12 U.S.C. § 1433 (federal home loan banks); 12 U.S.C. § 1441a(g) (Resolution Trust Corp.); 12 U.S.C. § 1452(d) (Federal Home Loan Mortgage Corp.); 12 U.S.C. § 1723a(c) (Government Nat'l Mortgage Ass'n and Federal National Mortgage Ass'n); 12 U.S.C. § 1749bbb-20 (National Insurance Development Fund); 12 U.S.C. § 1768 (federal credit unions); 12 U.S.C. § 1795k(a) (Central Liquidity Facility); 12 U.S.C. § 1825 (Federal Deposit Ins. Corp.); 12 U.S.C. § 2290 (Federal Financing Bank); 12 U.S.C. § 3019 (Nat'l Consumer Cooperative Bank); 15 U.S.C. § 713a-5 (Commodity Credit Corporation); 15 U.S.C. § 78kkk(e) (Securities Investor Protection Corp.); 20 U.S.C. § 1087-2(b)(2) (Student Loan Marketing Ass'n); 42 U.S.C. § 8102(d) (Neighborhood Reinvestment Corp.). By contrast, in other instances Congress has expressly exempted federal instrumentalities from property taxes. *See, e.g.*, 16 U.S.C.A. § 191 (National Park Foundation); 16 U.S.C. § 583j-2(e)(3) (West Supp. 2000) (National Forest Foundation); 22 U.S.C.A. 2124c(j) (West Supp. 2000) (Rural Tourism Development Foundation). *See also* 49 U.S.C. § 24301(l) (partial and conditional exemption for Amtrak). Congress' concern for preserving the ability of states to obtain revenue is so great that in some instances where the federal instrumentality is made exempt from property tax, Congress has authorized payments in lieu of taxes. *E.g.*, 7 U.S.C. § 941(c) (Rural Telephone Bank); 16 U.S.C. § 831l (Tenn. Valley Auth.).



to *any* state or local tax. That result is "implausible." *Davis*, 489 U.S. at 809 (confirming waiver though "Congress could perhaps have used more precise language," where argument against waiver was, in context, "implausible"). This Court should thus be "unconvinced that the contrast between the [pre-1985] express [but contingent] waiver of immunity and the [1985 amendment's partial] silence on the subject suggests that Congress intended to repeal the waiver in the [prior] act and thus to diametrically change course by implicitly barring state taxation." *Cotton Petroleum Corp. v. New Mexico*, 490 U.S. 163, 182 (1989).

## CONCLUSION

Petitioner respectfully requests this Court to reverse the judgment of the Missouri Supreme Court and to render judgment for Petitioner.

Respectfully submitted,

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